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UniCredit S.p.A. (UNCRY) Q4 2023 Earnings Call Transcript

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Q4: 2024-02-05 Earnings Summary

EPS of $0.36 misses by $0.18 | Revenue of $6.42B (3.31% Y/Y) beats by $394.03M

UniCredit S.p.A. (OTCPK:UNCRY) Q4 2023 Earnings Conference Call February 5, 2024 4:00 AM ET

Company Participants

Magda Palczynska - Head, IR
Andrea Orcel - CEO
Stefano Porro - CFO

Conference Call Participants

Antonio Reale - Bank of America
Andrea Filtri - Mediobanca
Britta Schmidt - Autonomous Research
Chris Hallam - Goldman Sachs
Pamela Zuluaga - Morgan Stanley
Delphine Lee - JPMorgan
Hugo Cruz - KBW
Marco Nicolai - Jefferies

Operator

Good morning, ladies and gentlemen. Before I hand over to Magda Palczynska, Head of Investor Relations, a reminder that today's call is being recorded. Madam, you may begin.

Magda Palczynska

Good morning, and welcome to UniCredit's Fourth Quarter and Full Year 2023 Results Conference Call. Andrea Orcel, our CEO, will take you through the results. This will be followed by a Q&A session with Andrea and Stefano Porro, our CFO. Please limit yourself to two questions.

With that, I will hand over to Andrea.

Andrea Orcel

Good morning and thank you for joining us. Today, we will walk you through what you have achieved thanks to our UniCredit Unlocked plan, our goals and our outlook for 2024. I have always stated that my ambition is to build a bank that is strongly grounded in the right principles and values, one that delivers long-term quality growth and value for all our stakeholders, our shareholders, our employees, our clients and our communities. As we report our 12th consecutive quarter of quality profitable growth across all regions, I can proudly say that in these last three years we have fulfilled this ambition.

For our shareholders, we delivered quality growth, operational and capital excellence, sustainable profitability, capital generation and distributions, all underpinned by strong capitalization, liquidity and asset quality. For our employees, we have focused on providing a motivating vision, a rewarding and merit-based environment, a culture to which they identify and ultimately pride in what we are achieving. And for our clients and community, they are at the heart of everything we do. We have improved the quality of service and support we provide, offering best-in-class product through diversified, integrated and strengthened channels. This commitment to delivering and pursuing excellence has been our guiding principle and driven all that we have done so far and it will continue to be our focus as we move ahead.

UniCredit had its best year ever in 2023, the culmination of a three-year journey which delivered for the present while transforming our bank and preparing for the future. We will review our past accomplishments and look ahead to 2024 and beyond, where our sights are set on new heights. This is the year we grew our net profit to €8.6 billion, up 54% while continuing to invest in the future and expensing €1.1 billion of integration costs. Without these, our net profit would have been €9.5 billion. We delivered a record return on tangible equity of 16.6%, 5.8 points higher than last year, or 20.5% with a CT1 ratio of 13% adjusting for our notable excess capital.

Fourth quarter was much better than expected, with net profit up 19% despite higher integration costs to secure our future. Without them, net profit would have been up 37%. We generated €12 billion in capital organically this year, underpinning our proposed distribution of €8.6 billion, or 100% of net profit, €3 billion dividend and €5.5 billion share buyback, while reinforcing our CT1 ratio by 100 basis points to 15.9%. Following new EBA rules, we adjusted Q4 CT1 and will continue to adjust going forward as we accrue distribution, both cash and share buyback. Our cumulative past three years distribution exceeds €17.5 billion, more than our market cap at the beginning of 2021.

At the same time, we increased CT1 by circa €10 billion in the period. Our per share growth continues to be industry leading, with EPS up 74%, DPS 80%, and tangible book per share up 17% this year. The quality of such growth is underscored by the progress on our three financial levers and a 12% reduction in share count over the year, 30% reduction since the beginning of 2021.

In 2024, we aim to maintain net profit broadly in line with 2023 record level, normalizing our best year ever while further improving the quality of our results across the P&L, delivering double digit growth in EPS and DPS. We expect the tailwind from interest rates and cost of risk to gradually fade. The impact from continuing to scale down Russia while our fees, which have grown to represent 32% of our revenues, should further increase their weight.

As we work to deliver these results, we will reward our shareholders with outside calendar year distribution of approximately €10 billion. We consider 2024 the start of a second phase of UniCredit Unlocked, rooted in the same vision, the same strategy and mostly the same levers as we continue our transformation. We will defend our profitability and the leadership achieved in operational and capital efficiency as well as cost of risk. We will strive to further improve the quality of our results, continuing to deploy our capital profitably while growing our capital-light businesses. We shall strive to sustain best-in-class distribution while strengthening our bank and continue to deliver value for investors through substantial earnings and dividend per share growth.

Let me now take you through UniCredit's best year ever, a testament to our commitment to excellence and our ability to adapt to changing market conditions. 2023 has been an exceptional year for UniCredit, with a stronger-than-expected fourth quarter in which we took the opportunity to absorb even more integration costs than anticipated. Our key metrics highlight the outstanding performance across our three financial levers.

Net revenue increased 26% to €23.2 billion, with gross revenue up 17%. We have continued to improve our operational efficiency, reducing costs by 1% to €9.47 billion, while absorbing inflation and investment. Our cost-income ratio has further dropped by 7.2 percentage points to 39.7% for the year. Similarly, we have continued to improve our capital efficiency, with RWA decreasing 2% to €284.5 billion, with net revenue to RWAs reaching 7.9% up 2.1 points.

We reached a record return on tangible equity of 16.6%, notwithstanding €1.1 billion of integration costs and a significant capital buffer. Indeed, our underlying return on tangible equity at 13% CT1 ratio reached 20.5%, 22.4% if we excluded integration costs. All these lead to €12 billion or 389 basis points of organic capital generation, underpinning our proposed increased distribution of €8.6 billion or 100% of 2023 net profit.

Let me now take you through the main item of our P&L in greater detail. We report a significant increase in net revenues, growing 26% year-over-year. This was driven by excellent net interest income and resilient fees, while our cost of risk remained significantly lower than our guidance of 20 to 25 basis points through the cycle. Our trading revenues continue to show resiliency and stability as primarily driven by client business.

Our NII grew 31% year-over-year and was sequentially flat in the quarter, driven by rates rising 218 basis points on average in the year and 21 basis points in the quarter across our footprint, coupled by strict pass-through management, which reached 28% in Q4 and averaged at 25% in the full year. We continue our focus on quality risk adjusted, simplified EVA positive origination, profitable and capital efficient client business rather than value-destroying volumes, which together with subdued loan demand led to client volume dropping €8.5 billion in the quarter. The rise in customer deposit rates was small with clients continuing to shift their savings into assets under custody products. However, our already strong liquidity position improved, with LCR increasing to above 145% and loans to deposit ratio decreasing to 86%.

Our NII sensitivity is updated to €130 million per percentage point change of deposit beta and €140 million per 25 basis points change of the ECB deposit facility rate. We view NII and cost of risk as intimately linked, both in the way that we look at our numbers and the way we manage our franchise and our KPIs. These numbers demonstrate what we have said quarter after quarter. We have a robust and high-quality credit portfolio at €428 billion with a low default rate, a very meaningful reduction of NPE to €11.7 billion with improved quality mix and coverage, as well as a lower expected loss on new business, confirming our vigilant approach towards new origination.

The last 12 quarters show a structurally lower and less volatile underlying cost of risk net of overlays in Russia, at an average of 16 basis points and always below 22, versus approximately 60 basis points on average from 17 to 19. This transform and strong asset quality underpins our 2023 cost of risk of 12 basis points, 28 basis points in the quarter as we took the opportunity to further build up our market-leading overlays and provision to protect or further propel our future results. We have and will continue to make substantial progress in our fee line. Notwithstanding consistent macro headwinds, we have grown our fees each and every year since 2021. We've compounded annual growth rate of 2% from 2021 to 2023 once we exclude the impact from current account fees and accelerated securitization cost.

In 2023, fees grew 1% excluding €180 million reduction in current account fees in Italy to the benefit of our clients and higher securitization costs. Today, UniCredit fee structure is well diversified. It is balanced with a top tier fee to revenue ratio of 32.3%. Full potential from past and future investment as the impact from internalization is yet to be realized.

Despite inflation across our geographic footprint and investment in our people, franchise and technology, we have been able to reduce cost 3% in a targeted fashion between 2021 and 2023. Growth of such investment and inflation, our costs would have dropped 13%. The fourth quarter of 2023 saw [Indiscernible] flat year-on-year in spite of a significant increase in our bonus pool. This is evidence in our commitment to paying for performance and recognition of the hard work of our people. Our focus on profitable capital deployment led to a net revenue to risk-weighted asset ratio increase to 7.9% in 2023, up from 5% in 2021. We generated 389 business points of capital organically in 2023, or €12 billion, well above our net profit, leveraging our quality focus and excellent portfolio management with proactive RWA management.

Risk-weighted assets stood at circa €285 billion, down almost €25 billion in the year. In 2023, UniCredit CT1 ratio increased almost 100 business points from 14.91% to 15.89%, showing our ability to distribute capital whilst continuing to substantially strengthen our capitalization. Over the last three years, our CT1 ratio has grown despite absorbing business requirements and substantial regulatory headwinds and returning €17.6 billion to our shareholders.

Let me now outline our results through the prism of our business, starting with client solutions. Our factories generated €9.9 billion in 2023, of which fees accounted for 64%. This is a 1% rise from the previous year if we leave out Russia, which we continue to scale down, showing the steady performance of our banks, backed by our factories in spite of challenging market conditions.

Corporate solutions brought in a revenue of €4.9 billion, a decline of 6% from the previous year, mainly due to the cutback of the Russian business and TLTRO, without which we would have been flat. Within corporate solutions, advisory and capital markets were up 11% and trade and correspondent banking 5%, as they both continue to leverage our unique footprint.

Deals of note include the Eurogroup, L'Automatica, [ph] Ferretti IPOs and Upower [ph] Leverage Buyout. Payments increased 12% driven by NII growth, boosted by our better leveraging of our European presence and recent investment in the business. Please remember that 90% of payments revenues are fee driven. Individual solutions still face a difficult macro environment leading to a 4% drop. However, we see positive signs in the growth of managed funds and especially in non-CPI protection, which was up 40% year-on-year.

Our Italian business delivered another quarter of outstanding results. €5.6 billion of profit before tax, up 29% year-over-year. Net revenue reached €10.5 billion, up 19% with gross revenues aligned. Net interest income grew 50% whilst fees were almost flat when excluding current account fee reduction done for the benefit of our clients and securitization cost. Cost of risk remained low at 22 basis points, stable at 19 basis points in the quarter.

Cost decreased by 1.8% leading to a cost income ratio of 35.8%, and down 7.8 points year-on-year, with continued focus on shrinking non-business activities and optimizing processes also through technology. Our focus on capital efficiency improved net revenue to RWA by 2.5 points to 9.3% in Italy, with an increase of ROAC by 8.5 points to 25.7%. Italy generated 168 basis points of €5.2 billion of capital organically this year. Significant progress has been made industrially. We launched 28 one market funds. We hired over 600 people while shrinking non-business staff by 700. We provided 1.2 million hours of training through UniCredit University to our staff.

Finally, we continue to invest in our distribution channel, including by refurbishing our branches and launching buddy R-Evolution. We have remained steadfast in our commitment to supporting individuals, households and businesses investing €10 billion euros through UniCredit per l'Italia. All these efforts have been recognized with UniCredit being named Bank of the Year Italy 2023 by the banker.

Our German franchise achieved its best result in over a decade, reaching profit before tax of €2.1 billion up 18% year-over-year. Net revenue reached €5.3 billion, increasing 13% with gross revenue up 8%. NII was up 4% and fees 1%. Cost of risk of 14 basis points was down 16 basis points versus 2022. Germany showcased operating efficiency, reducing its cost base by 4% whilst hiring an additional 320 full time equivalent employees in the business. This resulted in a cost income ratio reduction of 5.5 points to 44.3%.

Our focus on capital efficiency improved net revenue over RWA by 1.4 points to 6.9% in Germany, leading to a return on allocated capital of 16.1%, an increase of 5.2 points. Germany generated 98 basis points of €3 billion of capital organically this year. These results were propelled by our ongoing industrial transformation where we are investing in harmonizing and consolidating our training activities and technology. Banks were being an example of an enhancement to our digital offering. We have also made available 24 different onemarkets Funds in the country.

Central Europe delivered excellent performance in the year with profit before tax up 62%, reaching a total of €2.2 billion. Net revenue reached €4.2 billion, increasing 27% with gross revenue up 24%. NII increased 25%. Fees remain flat, net of higher acquisition cost in the Czech Republic. Cost of risk reduced to 4 basis points.

Costs remain broadly stable despite inflation and investment and cost-income ratio decreased by 8.8 points to 38.1%. Our disciplined approach on RWA continued across countries. Net revenue to RWA was up 1.4 points to 6.9%. ROAC reached 21%, up 6.7 points. Central Europe generated 62 basis points, or €1.9 billion of capital organically this year.

In addition to strong financial results, we are progressively rolling out 23 onemarket Funds in Austria, 16 in the Czech Republic, Hungary and Slovenia. And we are proud to have issued the inaugural green mortgage-covered bond in the Czech Republic and led the third series of green bonds on the Budapest Stock Exchange.

Eastern Europe. Eastern Europe confirmed its consistent profitability and demonstrated its role as a major growth engine for the group, with profit before tax almost doubling to reach €1.7 billion. Net revenue was up 48% to €2.7 billion, with gross revenue increasing 30%. This was driven by NII up 47%, fees up 3.8%, and a net reversal of LLPs with negative cost of risk of minus 22 basis points.

Cost-income ratio decreased by 8 points to 32.9%. Costs increased by 4.9%, substantially below inflation. Our approach towards capital excellence moved net revenue to RWA up 3.1 points to 9.6%. ROAC increased 17.7 points to 36.9%. Eastern Europe generated 39 basis points, or €1.2 billion of capital organically this year. The region is continuing its industrial transformation to support its present and future financial performance. We introduced an end-to-end digital process on overdraft and credit cards, as well as a voicebot in Croatia, to better serve our clients quickly and efficiently.

Our retail offering was revamped in Romania, resulting in a market share increase of approximately 80 basis points year-over-year. We also began to exploit the synergies resulting from the merger with Alfa Bank. Our onemarket Fund offering is already available in Bulgaria, with 16 funds, and soon to be launched in Romania. These actions led us to be awarded as the best bank in Bosnia and Herzegovina, Bulgaria and Croatia, and best mobile bank app in Bosnia Mostar.

2023 was not a standalone achievement, but rather the result of a three-year journey. I will now briefly guide you through the factors that underpin and sustain our outstanding performance. At the core of our journey lies our unique vision and winning strategy, underpinned by our industrial transformation, all guided by our shared principles and values.

Three years ago, UniCredit was falling short when it came to serving its clients. A siloed model, burdened by bureaucracy, with a corporate center that had lost its focus on the client. We have redefined our operating model, putting clients back at the center of the bank's strategy and operation, to unlock our inherent potential and deliver value for all our stakeholders. We are rebuilding UniCredit block by block, that will result in long-term, sustainable, profitable growth. We are empowering and unifying our team through a common vision and a clear culture, promoting ownership, accountability and learning from mistakes. We are all parts, working in lockstep, with our purpose and values as the lynchpin. We are simplifying and delayering, creating a leaner, faster and efficient structure that cultivates empowerment within a clear framework.

We are rationalizing and strengthening our partnership and our approach to procurement, leveraging group scale and bargaining power to build long-lasting relationships with our suppliers. We continue to invest in our people on the front line, distribution channels, products and in our franchise, with full value yet to be realized. We are modernizing and enhancing our digital and data capabilities, taking back control of core competencies, streamlining and enhancing our digital organization and standardizing and modernizing our technology.

As a result, UniCredit has gone from laggard to leader, both in terms of its model and its financial performance. Since the unveiling of UniCredit Unlocked, we have adapted to a changing environment to deliver unmatched value to our stakeholders, consistently over the last three years. Our financials have been excellent, with our 2023 return on tangible equity and net profit increasing respectively over 3x and 2.6x versus the 2017-19 average. We have generated over €27 billion of capital organically in the 2021-23 period, supporting a total distribution of €17.6 billion above our initial market cap, while substantially increasing our CT1 ratio.

Our 2023 EPS, DPS, and tangible book per share are up 3.1x, 9x, and 46% respectively, versus the average of 17-19. Our total shareholder returns have exceeded the peer group 3.5x over the last three years, whilst we have continued to build lines of defence and invest for the future. While the future is still uncertain and the challenge is significant, there is still meaningful value to be unlocked and we face the future with confidence.

Looking to the future, 2024 is a normalization year. We should absorb most or all of the headwinds facing us by further improving the quality of our earnings, our operation and capital efficiency and risk-taking, while greatly rewarding the investors willing to embark with us on the next phase of our journey. We expect NII to face headwinds as deposit pass-through continues to increase. We stand firm on profitability rather than volumes, and continue to scale down Russia, with an impact estimated at €300 million, partly upset by circa €400 million positive impact from our replicating portfolio.

Our cost of risk should increase from an all-time low of 12 basis points, but still remain below 20 basis points. We expect fees to grow by a few hundred million, thanks to our investment and more favourable environment. Trading should normalize, also in light of the assumed euro zone rate reduction during 2024, all resulting in net revenue of around €22.5 billion, based on our underlying assumption. The continued scaling down of Russia should account for roughly half of the gap with 2023.

We will drive our costs down further. This is while absorbing the effect of inflation and contract renegotiation through the exit financed by our integration costs, and supported by continued streamlining and simplification. Our non-operating items deserve a special mention, as they shall significantly reduce due to the integration costs that total €1.1 billion in 2023, trending to zero, and systemic charges reducing by more than €200 million.

As such, we expect net profit to remain broadly in line with 2023 level, with improved P&L quality. Return on tangible equity at circa 16.5%, and organic capital generation to exceed 300 basis points, all underpinning sustained distribution pre-NE capital usage. We are aiming for double-digit growth in our EPS and DPS. We intend to reward investors who embark with us on the next phase of our journey with circa €10 billion 2024 calendar year distributions. The sum of €7.2 billion of remaining 2023 distribution, after the 1.4 billion share buyback already executed in 2022, and the introduction of an interim distribution of around 40% of our expected 2024 distribution to be executed in the fourth quarter or in October.

Around €4.3 billion will be in cash, leading to a dividend yield of approximately 10%, an expected DPS growth of more than 2.5 times, and around 5.8 billion share buyback, more than 20% higher than last year, a total distribution yield above 20%. Looking beyond 2024, the second phase of UniCredit Unlocked entails the continuation of our vision, of our strategy, driving further achievements. We have transformed ourselves and as such are comfortable committing to continuing to do so to deliver significant value, quality and predictability over the long-term.

We are uniquely positioned to continue outperforming, delivering sustainable, outstanding profitability and distribution in 2024 and beyond. We face the future with optimism. We have anticipated the main expected headwinds and taken steps to address them. Our profitability is underpinned by targeted, proactive action that will pay dividends. In the face of pressure on NII, we are maintaining our focus on quality, not volume. With our fee-to-revenue now aligned with top-tier peers and set to grow further.

We have substantial P&L buffers and provision, a high-quality credit portfolio with low non-performing exposure coupled with overlays of €1.8 billion, €1.1 billion in integration costs trending to zero, and a reduction of over €200 million in systemic charges. The above supports us in an uncertain macro with changing rate dynamics, coupled with a best-in-class capital generation, they enable us to maintain our bottom-line profitability and outsize distribution without denting capital, which however remain well in excess of our target and shall be used going forward.

Finally, we sit on a bolted balance sheet with strong asset quality, low and stable cost of risk, leading CT1 ratio and healthy liquidity ratio. When we look at our trajectory and performance over the last three years, peculiarities emerge regarding how the market perceives us. We are less dependent on interest rates than sometimes assumed. Our NII growth is aligned with our European peer group average. We benefited less versus Italian peer due to our geographic diversification and an approach based on profitability rather than volume. We are much more fee-driven than people perceive and are among the top-tier banks in terms of fee-to-revenues. We have a diversified fee base with future potential from recent investment, including an additional €1.4 billion in fees at run rate from our best-in-class product factories. It is worth noting that a significant portion of this fee growth is locked in. It is not dependent on market dynamics, rather a function of ongoing managerial actions linked to internalization of value chain in asset management, internalization of life insurance, renegotiation of main supplier contracts across value chain and action in payment and advisory and capital markets.

These slides present the details of UniCredit fee growth consistent with the information shown in the Q3 results presentation. As such, I won't spend time discussing it now as I have already done so at Q3.

Before I open for questions, I would leave you with five key takeaways. Firstly, we have delivered outstanding profitability, significantly up year-on-year, well above expectations. Secondly, our capital generation and distribution continue to be best-in-class. Thirdly, EPS, DPS and tangible book value per share growth are unparalleled, underpinned by continued progress across our three financial levers, coupled with substantial share buyback. Fourth, Phase 1 of UniCredit Unlocked is effectively completed one year in advance, beating all KPIs, resulting in a transformed bank. The foundations for Phase 2 are set and rooted in the same philosophy.

And finally, we have a clear direction of travel. In 2024, we expect to normalize 2023 record profitability, improve the quality of our earnings, while delivering record calendar year distribution of circa €10 billion, and continue to grow EPS and DPS significantly.

Thank you, and I'll now open for questions.

Question-and-Answer Session

Operator

Thank you. [Operator Instructions] The first question is from Antonio Reale, Bank of America. Please go ahead.

Antonio Reale

Good morning, everyone. It's Antonio from Bank of America. Two questions for me, please. The first one on the outlook for capital distribution and the second one on your guidance for this year, perhaps with a focus on NII. So starting with the first one, if I think back when UniCredit first launched a buyback program about three years ago, that came with a signaling effect of sort of balance sheet strength, suggesting the cleanup and the restructuring journey had been completed.

Today, nobody seems to give much attention to balance sheet strength, and it's all about sustainability of earnings. Now, you're lifting dividend payouts to 40% with a commitment to pay at least 90% of earnings before 81 in cash, which is a welcome change in the definition. What makes you comfortable that this can be sustained and why do you think this is the right mix of capital distribution? That's my first one.

The second is to do with your four-year guidance, specifically on NII. I mean, you're guiding to be broadly in line to this year, also in 2024, so close to €8.6 billion. That consensus has some catching up to do. Slide 20, I think you provide quite a bit of qualitative color on the key drivers. Can we talk about this in more detail, please, and particularly on the outlook for NII in 2024, and if possible, your assumptions or your early thoughts about 2025? You're less sensitive than Italian crystal rates, so it would be great to understand the moving parts on NII from here. Thank you.

Andrea Orcel

Okay, I'll take the first question, and Stefano will take the second one, and we'll integrate each other. So, on distributions, what we have done this year is two things. One, we have aligned to new EB8 guidelines that require everybody to express distribution as a percentage of net income. And we are saying that going forward, we commit to distribute an amount of net profit or net income which is equal or in excess of 90%. We have put, because we continue to believe that what drives our distribution is organic capital generation, not net profit. We continue to put a cap on the overall distributions at 100% of organic capital generation. So, it acts as a cap to, for the time being, keep us honest at that level.

By definition, if we do that, we are recurrent, we are sustainable, because it means that year-after-year, what we distribute is what we can afford, and we do not use the excess capital on the ordinary to fund the distribution. That does not mean we will not distribute the excess capital. It just means that in the ordinary distribution we are talking about here, we're not including the excess capital.

The second thing is we have had a relatively low payout ratio in terms of dividends in the past few years, at 35% of net profit post 81 in cashes. And we have done so, one, because we wanted to be absolutely certain that our transformation was bolted, and secondly, because we considered our shares to be such a good bargain for us to buy back. As we move forward, and as a number of investors have highlighted that they would like an improvement in our cash yield, we've done two things. One, we're now calculating the payout before 81 in cashes. That has a significant impact. And secondly, we are increasing our payout to 40%. That does not mean that we will not increase it further, but at the moment, that's the number.

In addition to that, and that's the third point, as we are now at a significant level of distribution, we are smoothing the distribution by considering an interim distribution in October that will be equal to 40% of the distribution anticipated the following year. And therefore, as the year in which this happens, the total distribution in the calendar year will be circa, or depending on how we do, in excess of €10 billion, of which a significant portion in cash.

Stefano Porro

So, net interest income, let's start from 2024. So, key assumptions. Rates, assumption of average rates of 2024 equal to 2023. We are assuming an ECB rate cut between May and June. The starting point of the arrival is around 3.9. We're expecting that in Q4, the arrival will be below 3%. With regards, the net interest income sensitivity connected to rates, as highlighted by Andrea, is lower than the previous quarter, so every 25 basis points is €140 million. We are expecting a further reduction of the sensitivity during the course of 2024. One of the important elements to be considered is that we have increased the size of the replicating portfolio. So, we move from around a little bit more than €170 billion during Q4, 2022, to around €190 billion at the end of the year. So, this has increased the contribution to the margin of the replicating portfolio, but has also reduced the net interest income sensitivity.

Second assumption is deposit pass-through, i.e., the ratio between the client rate and the average interbank rate. We closed around 25% for the full year of 2024. The average of Q4 was around 28%. We're assuming that the pass-through will go up during the course of the year, especially in the second half, when the rates will go down. The average that we're assuming is around 30%, so you can look at 23, average 25, 24, the average is 30%. As also highlighted by Andrea, the net interest income sensitivity deriving from deposit pass-through is around €130 million, coherent with the assumption that I told you in terms of rates.

What about GDP? GDP that we're assuming in the footprint is below 1. That's a very important element to consider the expected growth of the lending. We're expecting still a lending stock reduction in Italy, also in Germany, differently from Central and Eastern Europe where we're expecting a growth. This is one of the elements that will change during the course of 2025, when the GDP growth that we're expecting is around 1.5, with also some positive implication on the lending growth.

For 2024, the key drivers are the two that I mentioned. Average rate the same, deposit pass-through going up, replicating portfolio contribution €400 million, and as highlighted already in the speech by Andrea, a reduction of the contribution by Russia for around €300 million. We're not expecting meaningful impact deriving from the volumes and client spread trend.

On top of GDP, improvement in 2025 is fair to be assumed that the average rate in 2025 will be lower clearly than the average of 2024. You have the sensitivity, but please do consider that, as I told you before, we are expecting that net interest income sensitivity can be lower at the end of 2024 in comparison to the beginning of the year.

Antonio Reale

Thank you.

Operator

The next question is from Andrea Filtri, Mediobanca. Please go ahead.

Andrea Filtri

Thank you. You have led the way for the entire sector on share buybacks, and now you're doing it on total distribution. Now you have essentially hinted at a potential gradual increase in cash payouts. You have introduced interim, and you still have a very thick excess capital buffer. Do you think the journey on this front has ended? Are you at run rate, and are you comfortable with these levels with the change of the guard at the regulator? Thank you.

Andrea Orcel

Okay, so I think we're very comfortable with the distribution that we have. So from day one, we insisted that what drives distribution is capital generation. Fundamentally, very simply, what capital do you have at the beginning of the year? What capital do you have at the end of the year? And if you have an excess and you distribute that, then you're sustainable, you're current.

Of course, there is a period in which that capital generation is significantly in excess in the profitability, and then the net income. Then there is a phase where it converges to net income, and then at some point there will be a phase where it will be less than net income. UniCredit has been in the phase in the last three years where capital generation has been significantly in excess to net income.

As a result, notwithstanding distributing €17.6 billion to our shareholders, we increase our excess capital very materially. So if you look at the trend and you look at our expectation going forward, we're saying in excess of 300 business points on a profitability of broadly in line, which is about 8.6. So there is a beginning of convergence of the organic capital generation to the net profit, which we think will remain above over the next three years, but we will see what happens. But we think it will remain above. So allowing us to peg very strongly on net profit, our distribution, and we said equal or above to 90% to be, let's say, realistic or conservative with respect to where we are moving.

Then there is the question of where we will be at trend line. Well, if you go beyond three years, although I don't have a crystal ball, hopefully we will have even greater profitability. The organic capital generation will be close to net income but below, but because net income will be higher, we will be able to distribute similarly to what we distribute now. And I don't know exact landing because we need to look at that. When we look at the composition of what we're distributing, in the composition of what we're distributing, we've had shareholders that were very vocal on at this price by your shares. And we've had also shareholders would say, okay, but as you're trending towards stabilization or normalization, increase your payout because we want more dividend yield.

So we are responding to those shareholders by slightly increasing our payout. But it is clear, and I have said in other calls, that we will continue to increase the payout at some point, and 35 or now 40% is not the end game. We cannot be a bank that prides itself on generating through profitability outsized distribution and remaining with an under-peer payout ratio. So over time, we will progressively increase that percentage.

Now, I'll speak what is over time. It will be judged based on our share price evolution, are we stabilizing, are we normalizing, a lot of factors in there. But we're committed to increase it over time. Then you see the interim. Given the amount of distribution that we're doing, both in terms of dividend payout, but remember, we're still majority share buyback, we need to spread. Because otherwise, we create a situation where we're too concentrated on one part of a year and indeed in terms of dividend on one date, which is not the best thing in our opinion. Which is why we introduce the interim dividend by spreading the number over two parts of a year.

Finally, I think that with respect to our view, with respect to where we're going, we absolutely are comfortable that this direction of travel and the way we're stating it is consistent with regulatory expectations. And going forward, the only question mark that remains, that as I said, I will clarify after the AGM, because it's a commitment for the following three years and I don't want to anticipate anything, is what we will do with the excess capital.

If you ask me, now on an individual basis, that excess capital needs to be used. And it will be used either by complementing the distributions on an extraordinary basis, so we will have the ordinary number that we have just discussed, plus an underpin of excess capital return to our shareholders over a certain period of time. Or used in acquisition, if the terms and conditions, in particular pricing, leads us to be able to demonstrate to investors that as we focus on value, that acquisition fulfills that objective and benchmarks correctly with buying back our own shares. So far, we have not been able to do that, but I don't exclude that that is possible in the future.

Andrea Filtri

Thank you.

Operator

The next question is from Britta Schmidt with Autonomous Research. Please go ahead.

Britta Schmidt

Yes, thank you for taking my questions. Could you perhaps just comment on the fee and insurance side? I think you slightly upped the 1.4 billion benefits now from 1.2 billion previously. Can you give us a bit of an update of some of the statuses where on the payment strategy and also what timing are you thinking about for the restructuring of the asset management?

My second question will be on the expected loss and overlay usage. Where really do you see now your structural cost of risk in the longer term? And how and when do you expect to use the 1.8 billion overlays? And just as a clarification, just on Stefanos' comments on the deposit costs, does that mean that the deposit costs at year-end 2024 are going to be lower than the 1.2% in Q4 2023? Thank you.

Andrea Orcel

Okay, let me take the first part and then Stefano will come after me. So, first of all, the philosophy question, what do we do with overlays or with the excess provision we have created vis-à-vis benchmark? Well, it's a question of where we see the cycle. So, the overlays and the excess provision are there to protect us against the cycle or if our expectation and the expectation of the industry on the cycle are less negative to then be released as we should and therefore propel further our results. So, we have capacity in there.

When are we going to do that? Well, if you tell me when the back end of a cycle arrives in terms of risk, I will tell you when I will release them. At the moment, our anticipation, which may be right or wrong, is that we are going to see an increase in cost of risk gradually more visible in the second part of the year and in particular starting Q4, getting into 2025. Why? Just because you will have had the time on the rate increase, on all the challenges, the geopolitics to go through our clients and potentially you're going to see some increase in cost of risk. We are more optimistic than I think some are, but we are prepared for the worst.

So, assuming that in Q4 we see an increase and then it will continue in 2025, we have this 1.8 billion plus excess provision we have on a specific basis to make sure we deliver on the commitment we took to keep our cost of risk between 20 and 25. If the cycle is not like that, two things can happen. One, you see nothing at the end of 2024 and 2025, I doubt it, or you see much less. In any case, we are going to be obliged to release these overlays. Those overlays are there for specific reasons. They are not there to stay there. And therefore, in that case, our results and our cost of risk will trend significantly below the 20 to 25 as we release. So, that's in general how we look at it.

In general, on life insurance, and then I'll pass it on to Stefano, and on asset management, the strategy is still the same? On insurance, we were clear on two things. One, we would rationalize our partners and heavily tilt towards alliance. We've done exactly that. Secondly, we would internalize life insurance, which for us is unit linked primarily, if and when the Danish compromise was confirmed. It was. So, sometimes in 2025, we will internalize the life insurance unit linked as per contract by buying the insurance company that we share with one of our partners and concentrating there most of our unit linked and life insurance. That will have an impact on our rate income that Stefano can take you through.

Nothing has changed. The only thing that is changing more and more positively is that our progress on non-life insurance, in particularly ex-CPI, and in particularly in Italy, has been very, very positive. And we have converted quickly, and as you see, the volumes are going up very quickly, and we have a market share of new business in the mid-teens, which is quite good for us. And on asset management, I think it's not a restructuring.

As for many other things, it's a progressive improvement. It's an improvement that we started by improving the way we set our asset allocation, that we provide strategies that are consistent to that for our clients, that we improve the design, the selections, and use our bargaining power to buy products at a better price. And that allows us – we used to have a rough cut of making €1 on the value chain. We used to maintain low 60% of the value chain in-house. We've moved that over the last three years to low 70%, and we think we can get to low 80% in-house by doing what we have just said. When I tell you that one market is getting rolled out in all of these countries, this is part of our grabbing the value chain to a greater extent for UniCredit.

And this is a gradual movement that will continue to occur, and that has nothing to do with the market. If the market then bounces because of rates, that's on top. But this is what we're doing on our own value chain.

Stefano Porro

So, in relation to numbers, insurance. So, the insurance base for -- revenue base for this year, let's say, is around €900 million. The expected growth in terms of a run rate that we are aiming at is around €400 million. The growth is arriving from on one end, re-insourcing a part of the chain, but also to increase the revenues that are coming from the long life, both in relation to CPI and in relation to property and casualties.

So, the expectation is to have a double-digit growth in relation to both in the next three years. In relation to payments, the base is clearly higher, so it's around a couple of billion. The growth that we are expecting is around €300 million. In relation, let's say, the two categories where we are also expecting a CAGR that is around 10% are cards and acquiring.

With regards to overlays, we have slightly increased the overlays at year-end. We have slightly changed the composition of the overlays. Overall amount is 1.8. We need to use or to release in the next couple of years. What we cannot anticipate now is, let's say, how and when, if we look 2024, 2025, but in this couple of years, we don't believe there is another option, rather than releasing or utilizing if the overall evolution of the credit portfolio is worse than what we are currently expecting.

With regards to the deposit cost, at the end of 2024, I would differentiate between the different countries, because we have a different composition of site and term deposit depending on each country. So, the average of the group is 75% site, but if you look, for example, to Italy, we are at 95% site.

In general, we are expecting that if the rate dynamic is in line with our assumption, we will have a progressive reduction of the cost in the country where we have term deposits. While, for example, in countries where we have mainly site deposit, I believe this is unlikely. So, in relation to Italy, we believe that this is unlikely. We are not expecting a meaningful increase of the cost of the deposit, but a reduction is not very likely.

Andrea Orcel

Britta, let me add one thing, because I may not have addressed the full question. If you look on that slide that I didn't comment, the impact that we expect from fees, in Q3, we were talking about €1.2 billion at run rate. We have increased that to €1.4 billion at run rate. The €200 million difference is partially rounding, partially spread all over, but mostly driven by payments.

As we said, we will give you an update on that at the end of Q1, but the payment side of the equation will be approached in exactly the same way, block by block of the value chain, as we have approached asset management and insurance, and we are going to go to payment and do the same thing. As we do that, we should have, one, the benefit from higher focus than the market, but also the mechanical impact of potentially internalizing more, streamlining more, or doing other things in this direction.

Operator

The next question is from Chris Hallam with Goldman Sachs. Please go ahead.

Chris Hallam

Morning, everyone. Just two quick ones from me. First, on efficiencies, you managed to reduce costs by about 1% in Q3. That was when inflation was high, and you talked earlier about the underlying 13% drop excluding inflation. How should we think about the size of the cost savings or cost reduction we should expect to see this year, especially in light of the €1.1 billion of integration costs you took in 2023?

And then second, on volumes, as Stephanie mentioned earlier, the GDP outlook, but just what's driving the overall guidance for lower volumes year-over-year? How much of that is discipline on pricing and returns as opposed to overall market activity levels? And then, when would you expect to see volume growth coming back?

Andrea Orcel

On cost, a few things just not to induce you in error. The first thing is, with the exception of Central and Eastern Europe, but in particular Eastern Europe, but Central and Eastern Europe, most of the effect of inflation are backdated or at the tail. So, the impact of inflation for the Italian contract renegotiation is in 2024, is not in 2023. And many other contracts go in the same direction. So, the integration costs that we're taking are going to compensate the real effect in inflation that we anticipate in 2024 and 2025, not in 2023. What happened in 2023 was taken care of by the integration costs and what we did in 2021 and 2022, and so on and so forth.

So, there is some lag. So, while, yes, we took 1.1 billion in integration costs, it's also true that most of the inflation impact on the Western European, let's say, employee base is in 2024 and 2025, not in 2022 and 2023. Okay? So, that's point number one.

Point number two, costs are not only people. Costs are also non-people, and we still are at run rate on what we invest in technology, on what we invest in the build-up of our factories, on distribution channel integration, on hiring at the front end, as we shift people from the center to commercial activities and we streamline. So, while the, let's call it HR cost is declining, the non-HR cost is increasing, and it should, because we are investing in digital as we go forward. So, if you look at all of that and you pull it all together, I think this organization has delivered very good performance on cost by trending down every year between 21, 22, and 23, in spite of maintaining investment. And just to remind you, as we said that we were trending down a few percentage point, but that number becomes 13% if you eliminate the investment in technology, in new people, in the factories, etcetera, etcetera. These investments are continuing. We're not relenting from that.

So, I think that if this organization is able to take the cost in 2024 slightly lower than 2023, and as I said in another call in Q3, our ambition is to match or slightly overcome what we had in UniCredit Unlocked without all of this inflation when we started, and keep it there for, let's say, a couple of years. While we continue to invest in technology, in our front end, in refurbishing of our network, in new channels, in hiring, etcetera, etcetera, I think that's a good outcome, and I think you should bank that, not more.

I think the only thing, and then I'll pass it to Stefano. Look, I think at the moment, as you see, our real underlying return on equity, so our ROAC, is you can call it 20.5 or more if you take away the integration cost. But when we look at the deployment of our capital, we're not deploying our capital at 20% and above. We're deploying our capital, or the bar that we put, is at our cost of equity. Our cost of equity is 11% to 12%, the real one. So, if we have an 11% to 12% assumed return from the deployment of our capital, we do it, and if we do not, we do not. And I think that that discipline pays dividend in the long-term because that's what drives long-term profitability and distribution. Otherwise, it could drive volume, show you a nice dynamic on NII, probably a nice dynamic on net profit, a much less positive dynamic on profitability and on distributions.

So, we will continue in that direction. Obviously, when we look at clients, we look at clients. We don't look at lending. We look at the entire relationship. So, if you're a client sitting in our legacy portfolio and you've been there for years, and your returns are below our cost of equity, and we give you one last chance to align, if a client is not aligning, that's structural. And I think it is correct for us to gradually, orderly, de-emphasize that relationship. If instead, it's a new relationship, or it's a client that is aligning to our cost of equity or exceeding it, we will invest in the client and we will do it. But again, not a 20% return at 11. But I'll pass it to Stefano for more details.

Stefano Porro

Okay. So, I will take it first on cost. So, HR cost. Let's look to the key variables. So, the average FTEs, if we look at 2023, in comparison to the beginning of the year, are down for more than 5%. So, and just a couple of percentage points, if you look at Q4. The expectation is that we will have a further reduction, but at a slower pace. Solid drift is [Indiscernible]. The full impact of the Austrian contract was already there in 2023, fundamentally, but not the Italian one. And so, as a consequence of that, the solid drift increase in 2024 will be higher than 2023.

With regards to non-HR cost, we will see an increased level of IT cost, on one end. But on the other end, in comparison to 2023, we are expecting a reduction in the real estate cost. That will include action on the footprint, but also the energy-related cost that we are expecting to be lower in 2024, in comparison to 2023. On volumes, fundamentally, there are three components. Rates and GDP. Rates are high, and as a consequence of that, there is an impact on the demand. So, this will be there also during the course of at least the first half of this year. Then there is the GDP. I told you before, there is a differentiation. So, GDP of Italy and Germany, expectation is lower than 1. But then, if you look, Central Europe, it will be above 1. And Eastern Europe, it will be above 2. So, this is why also the expectation in terms of lending trend is differentiated by country.

The third topic, as already highlighted by Andrea, is the pricing. We do see pricing competition in many geographies, also by cooperative banks and so on. Considering that we go for profitable and quality growth, there is also part of the expectation that is depending from our strategy. This is especially on the corporate side. So, this is impacting a portion of, let's say, the lending, especially on the corporate side.

With regards to inflation, the inflation expectation for 2024, maybe that is an important driver. Because on our footprint, the inflation in 2023 was around 7%. In 2024, we are expecting to have 3%. This is not automatically translating in cost drift. The salary drift is impacted by what we will negotiate. Just to remind that the renegotiation for German contract is expected in the second part of 2024. So, not before this moment.

Operator

The next question is from Pamela Zuluaga with Morgan Stanley. Please, go ahead.

Pamela Zuluaga

Hello, good morning. Thank you very much. I want to ask you about your push for fees. Life insurance has suffered in Italy from a shift in the savings flows into BTP. What does this imply for your expectations on life growth now that you are planning on internalizing? Do you think this is a trend that will reverse soon? Maybe now with potential rate cuts?

Then, within the asset management fees, you are mostly a distributor of collective investment products. You say you want to optimize the value you retain from your distribution agreements. But, for example, your agreement with Amundi is still in force, I think, until 2027. So, should we expect a big part of this value retention strategy to materialize with some sort of delay? And if I may, as a follow-up.

So, the guidance for the 90% payout on flat net profit next year implies that distribution will be at least €7.7 billion against 2024 earnings. When you talk about the sustainability of this payout, would you also expect a sustainability of this sort of absolute amount? In the case the distribution cap of organic capital generation falls below net profit before the three years that you were mentioning, are you willing to use excess capital to top it up? Thank you.

Andrea Orcel

Okay, let me start with a second one because it's more straightforward. The answer is yes and yes. So, fundamentally, we have done a lot of work on what we can do in the next three years. We feel that the current levels of profitability are sustainable, plus minus, obviously, plus minus. With those levels of profitability and those levels of net income, and most importantly, organic capital generation at the levels that we are anticipating, let's say at least €7.7 billion is sustainable as an ordinary level of distribution.

Like any other organization, if our profitability starts dropping or organic capital generation starts dropping, it will go down. But that happens to anyone. If you ask me where I see going in the next three years, I think €7.7 billion is sustainable. As a minimum. Now, in addition to that, you said what about excess capital? It is clear that when you look at your distribution, you should be looking at two things. One is the profitability sustainable. I think with the lines of defense and the investments we have, it is.

Secondly, what happens if you miss? Everybody can miss. Well, we have a ton of excess capital, and at that point, we would chip in. And if we chip in, obviously, we can sustain it. Consider one thing, that if we were to deploy some of that excess capital acquiring something, the share count will be non-changing because we are using excess capital. We are not issuing new shares, but the net income would go up because we are buying net income effectively. So, it is another way of creating more generation of our distribution going forward. That is how we are looking at it.

The second thing is, and I will let Stefano add. So, with respect to life insurance or unit linked, yes, they suffered because of flows into BTPs. But at the same time, like the rest of asset management, they should come back. They should come back when rates normalize and things normalize. In general, given the levels at which we can buy back our joint ventures, we are comfortable that they add value even at the current level of flows. With respect to Amundi, Amundi does not provide all of our asset management. We have a substantial portion, 20%, 30%, depending, that is in inverted commas “free”.

Most of the value that we are creating on the value chain is focusing on that 20% 30% today. Beyond, we will see. We will see about our agreement with Amundi, etcetera. But I don't think it is an all or nothing between now and 2027. It is a progressive, with 2027 obviously being an important year as one of our key agreements is up for renegotiation.

Stefano Porro

Just to add on the life insurance, on the time horizon, we are not expecting a reverse when there will be the rate cut. We are expecting an improvement of the trend when the rates will normalize, i.e. not for 2024 but more for 2025.

Pamela Zuluaga

Great, thank you very much.

Operator

The next question is from Delphine Lee with JPMorgan. Please go ahead.

Delphine Lee

Good morning. Thanks for taking my questions. Just a few ones, a couple of ones. On net interest income, can I just ask this? I think before you were guiding to NII to decline moderately, you don't specify moderately and there is no precise guidance now. I am just kind of wondering, looking at your comments on the replicating portfolio or Russia, it seems that actually NII could still be resilient. I just wanted to have a bit more comment on that. Also, if you could just clarify on your rate sensitivity, the €150 million for 25 years, what is the assumption you are making on deposit beta?

Then my second question is more broadly on excess capital and M&A because now you are doing more than €6 billion of buyback per annum. I am just wondering, is the excess capital still based on a 13% CT1 level? How much capacity is there really for exceptional buybacks? Or do you feel like there is more pressure now to go the M&A route? Thank you.

Stefano Porro

On net interest income, we have not guided with specific numbers also because we have given you all the key ingredients. In relation to the ingredients, coming back to the ingredients, fundamentally, on one hand there is Russia, which is very important because the more we are reducing the exposure and we are scaling down Russia, the more we have an impact on net interest income, is €300 million. This is one very important component.

The second element is the deposit pass-through that we already commented before. Then I will arrive then to the sensitivity. The third one is the replicating portfolio. The replicating portfolio is there, is impacting. The contribution to the net interest income in 2024 has allowed around €400 million more compared to 2023. It has also reduced the net interest income sensitivity because increasing the stock of the replicating portfolio over time has also reduced our net interest income sensitivity. The sensitivity to rates moved from 150 to 140 and is coherent with the deposit beta that we have allotted. The deposit beta is in Q4 around 28% while the average for the year in terms of expectation is around 30%.

Andrea Orcel

With respect to share buybacks, yes, we take 12.5 to 13 as our target. It is the same target we had put in our plan of unique rate unlocked. It has not changed. Secondly, obviously, there is an impact from Balfour in 2025. That impact for us is about 80, 85 basis points which will reduce that excess at least nominally if we remain at 12.5%, 13% target. You can calculate what it is after that. Now, is there more pressure on M&A? I would put it differently.

There is less pressure on M&A given the results that we can continue to deliver internally but potentially there will be more opportunity if the divergence between results of winners and losers in the industry becomes more marked.

Delphine Lee

Thank you very much.

Operator

The next question is from Azzurra Guelfi with Citi. Please go ahead. Guelfi, we cannot hear you. Maybe your line is on mute. Guelfi, we still cannot hear you. Maybe your line is muted. The next question is from Hugo Cruz, KBW. Please go ahead.

Hugo Cruz

Hi, thank you very much for the time. I wanted to ask just two things. One was RWA optimization. If you could quantify how much you still have to do or how much you think you can do during 2024. And then a more broad question. Mr. Orcel, if it depended just on you, when would you like to leave your current role at UniCredit? Thank you.

Andrea Orcel

I'm just -- okay. So, RWA optimization, I will pass to Stefano on the numbers. But I think as we told you at the beginning, at the moment we're generating capital through two levers. Profitability, so net profit minus the cost of the business. Minus the capital we use to generate it. That capital, as we become more and more efficient on our revenue per RWA, decreases per unit of profit we generate. Obviously, the more fees and the more. And we go back to the question before. We deploy capital above our cost of equity. The more capital we generate per unit of net profit.

And the second part, which is more transitory. The, let's say, rendering efficient, managing the legacy portfolio. So, what we have, the 430 billion of portfolio that we have bringing it as much as possible above the cost of equity. That will always be there. But obviously, not even close to the amount that we have done in these three years. Gradually, it's coming off. So, we cannot generate 400 business points of capital on 12 billion of capital on 8.6 billion of net profit forever. I wish it was like that, but it's not.

So, gradually, it's coming off. And so, I do think that in 2024, it's going to still be. So, the contribution from that brings us above net profit in 2024, in terms of organic capital generation. We feel that that will happen also in 2025. And potentially in 2026, but we need to see. We will become, and are becoming more and more over time, in inverted commas, “net profit” dependent.

But, as we increase that net profit, and we increase the efficiency of our capital deployment with more fees, and more deployed above the cost of equity, the amount of distribution that we can distribute from that net profit continues to rise. And so, we hope that at the end, you almost won't see a change, because our net profit will be higher, and the percentage of net profit we distribute in distribution will be almost a continuation of where we would have landed you in the years prior to that.

But, it's a gradual course. If you wish, if we were to apply the same methodology to our targets or to our acquisition, or whatever, we then replenish what we're trying to do. But, for the time being, there is a finite life, and beyond that, Hugo, it's difficult. I would love.

So, with respect to the question, I would say, it's up to shareholder and more broadly stakeholders. But, I love the place here, and we're doing exceptionally well with a team that has given a lot, and therefore, I am fully committed.

Stefano Porro

So, some data points more on active portfolio management, and risk-based optimization. During 2023, we have done, if you look, securitization, active portfolio management, including all the activity on EVA negative clients, is more than 10 billion. If you look at our corporate portfolio at group level, the amount of EVA negative, let's say, is around 20 billion. It's clear that we will not do securitization, or not rolling over opposition of the amount, but still, we have some billions that we believe we can optimize during the course of both 2024 and 2025.

Hugo Cruz

Thank you very much.

Operator

The next question is from Marco Nicolai with Jefferies. Please go ahead.

Marco Nicolai

Hi, everyone. Thanks for taking my question. I've got two. One on costs. So, your headcount continues to shrink at a good pace, and given the restructuring costs you booked in 4Q, there is further room to go. So, I was wondering, what is driving these cuts? Is it more branches, rationalization? Is it head office? Is it IT investment benefits, or something else?

And the second question is on, again, NII. So, on Russia, I appreciate your guide for headwind in 2024, about 300 million less. However, if I look at the fourth quarter, NII was actually up Q-on-Q. So, how shall we think about Q-on-Q evolution on the Russian side? Thanks a lot.

Andrea Orcel

So, I'll take the cost, because the costs are completely connected to what we said since day one. This organization was highly centralized, and the level of center, non-business cost, administration, bureaucracy, call it whichever way you want to call it, was far exceeding what I think was the levels of average peers, and I still believe organization needs to go further. So, what we have done is embark in efficiencies that are very targeted. This is not a socialized efficiency. This is efficiency that attacks the area one by one, whereby redesigning processes. Take one that I used the first day I came here. We used to have in one of our countries 23 people to sign off on a mortgage. If we go to an end-to-end process, we don't need 23 people to sign off on a mortgage.

So, when we talk about organization streamlining, delaying, process redesign, change of way of working, what we're talking about is going into the mechanics or the industrial of every process, the way we do business, the way we sign off business, etcetera, rethinking it, redesigning it, making it more efficient, improving the speed, and reducing the cost of doing it. That part does not touch the front, does not touch the factories, does not touch digital. Actually, it does touch digital in one way, and I will explain to you how. That part effectively not only reduces cost and increases speed, but also releases a lot of energy because the people who are doing anything, something, i.e., in commercial, have a lot less weight to carry on their shoulders and can take decision and can move much quicker.

So, that's where we have targeted. So, if I take your list, head office, absolutely, IT, I would say, not the IT you think. We used to have more than 50% of our IT organization that had non-engineering software developer coding roles. In best-in-class organization, that number is below 20%. So, we have taken away that, so the layers, or are taking away that, and are reinvesting in the one that matters to transform our organization, which is software engineers, etcetera, etcetera. That applies to the entire organization. So, we're taking away and shrinking the bureaucracy to what is needed, and invest in hiring or technology or any other thing that we need to make our business more efficient. So, it's a targeted cost reduction to finance the rest. As you can imagine, at some point, we reach the end. We're not at the end yet, but that's where we're going.

Stefano Porro

Russia, Q4, top line, impacted by the positive effect deriving from the sale of a cross-border position. That's on one, positive impact on the revenue. Second, net interest income trend impacted by the effects trend. So, we need to look at that with a pinch of salt, because when there is, let's say, a rubble appreciation, you should also take that into consideration. So, if you look at cost and effects, the expectation is that the net interest income will be lower already in Q1, 24, in comparison to Q4, 23.

Andrea Orcel

Just to be clear, Marco, we always said that we were conservative in our provisioning for Russia. So, obviously, if we're conservative in our provision and we sell a cross-border position well within our metrics or well within provision, we actually create a gain. But you need to take that away to look at the trend line of the underlying in Russia.

Marco Nicolai

Yes, okay. Thanks a lot. That's very clear.

Operator

So, gentlemen that was the last question. And the floor is back to the management for any closing remarks.

Andrea Orcel

So, thank you everyone for your time. And thank you for staying with us. And we'll see you all later. Thank you. Bye-bye.

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